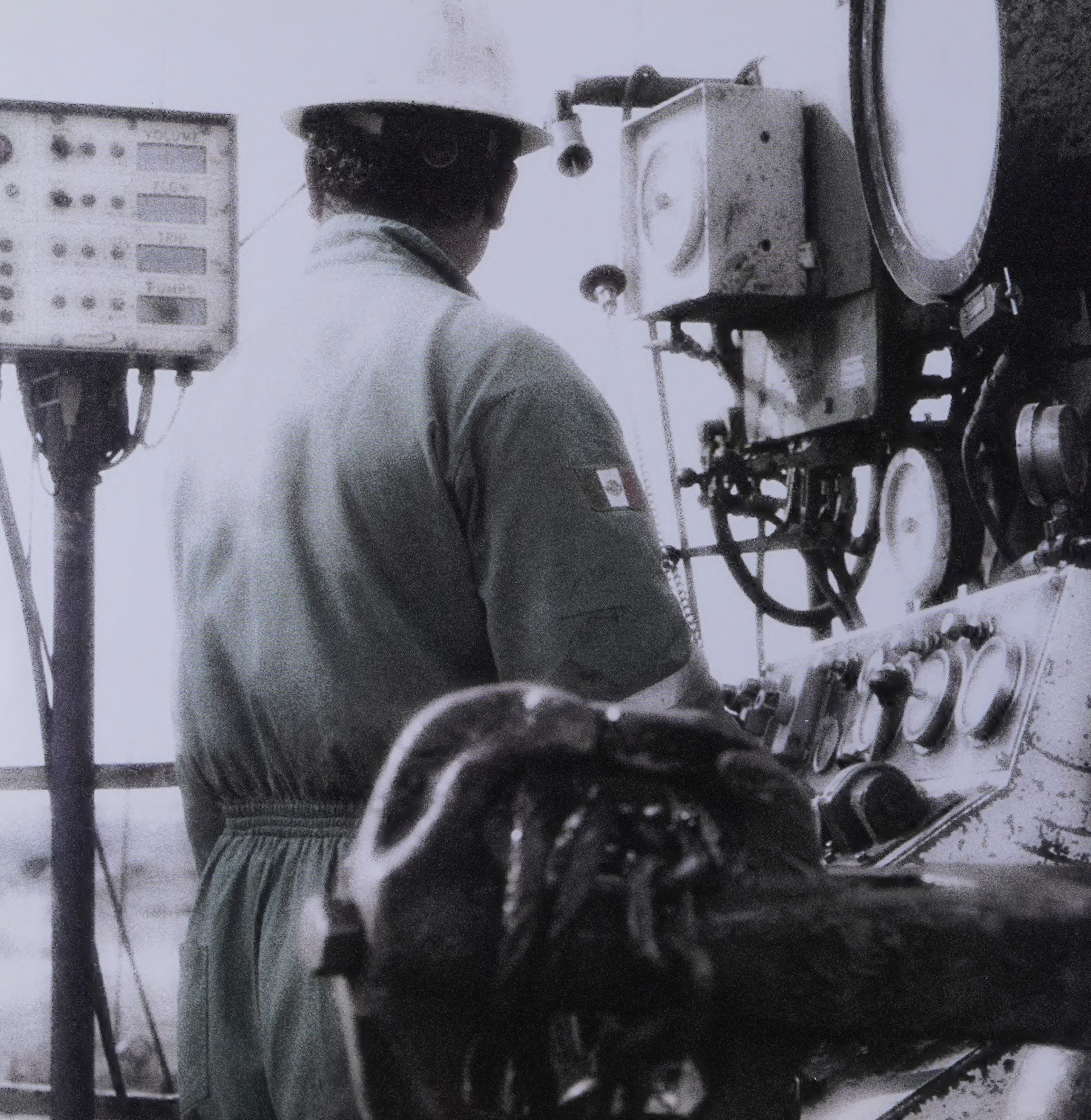
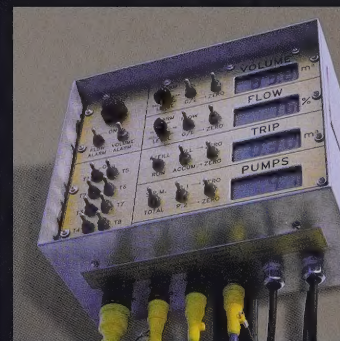
PASON SYSTEMS INC. – ANNUAL REPORT

2002

Pason delivers...


pason

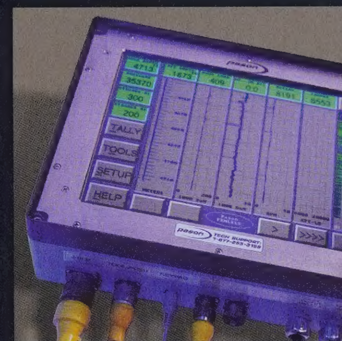




Pason delivers the integrated

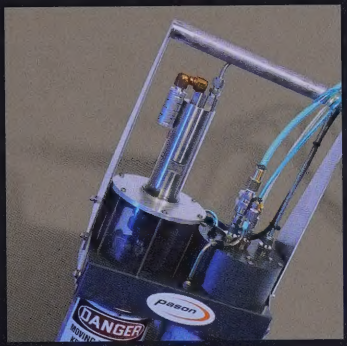
Pason's integrated equipment is designed with optimum ergonomics to capture the "vital signs" or sensor information of the drilling rig. ☐ The Pit Volume Totalizer (PVT) is Pason's proprietary solution for the detection and early warning of "kicks" that are caused by hydrocarbons entering the wellbore under high pressure and expanding as they migrate to the surface. Operating in conjunction with the Company's Electronic Drilling Recorder, Pason's PVT is acknowledged as the leader in dependability and functionality, and is an essential safety addition to all drilling operations.

TALLY
TOOLS
SETUP
HELP
pason



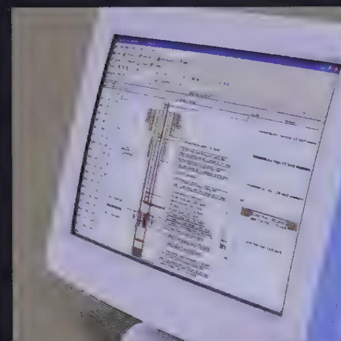
Pason delivers the integrated wellsite

All data is captured and displayed on the Pason EDR to assist wellsite operating personnel in optimizing drilling efficiency. □ Pason's Electronic Drilling Recorder (EDR) is a complete system of instrumentation and monitoring equipment that acts as a base for all data capture, data display and communications at the drilling wellsite. Each EDR system consists of a proprietary industrial computer, sensor set and junction box, together with a series of workstations connected via a Local Area Network in order to share real-time drilling information with all wellsite personnel. The Pason EDR is the envy of the industry and the cornerstone to which all subsequent Pason product offerings are leveraged.



delivers the integrated wellsite **instrumentation**

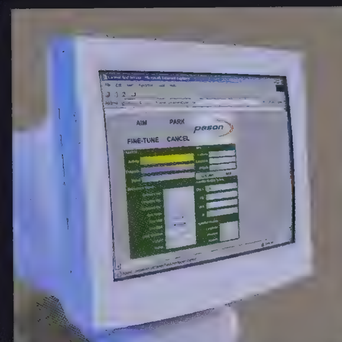
Despite a harsh operating environment and rough handling, Pason instrumentation is designed to provide industry leading ease of use and reliability. ☐ The Pason Total Gas System (TGAS) measures the total hydrocarbon gases (C1 through C5) exiting the wellbore and then calculates the lag time to show the formation depth where the gases were produced. A robust system capable of operating with a high degree of accuracy, Pason's TGAS provides the maximum amount of information with the minimum amount of maintenance in the most extreme of environmental conditions. This system is designed to operate with Pason's Electronic Drilling Recorder and as such, the information it provides can be viewed by any wellsite user via the data network.



he integrated wellsite instrumentation and data

The wellsite foreman can monitor all vital rig data from his command centre while reviewing reports created by Pason's custom software, thereby assisting him in making quicker and better informed drilling decisions. □ Pason WellView is a drilling data collection and reporting system that is the product of a partnership between Pason and Peloton Computer Enterprises. Pason WellView is deployed as an integrated addition to Pason's existing wellsite hardware. The module follows the Pason Electronic Drilling Recorder and the rigs on which it works so office drilling superintendents are no longer required to make special mobilization efforts for hardware, software or communications. All data is displayed in standard forms on Pason's Internet DataHub allowing rig personnel to save time and office users to receive better quality records.


pason

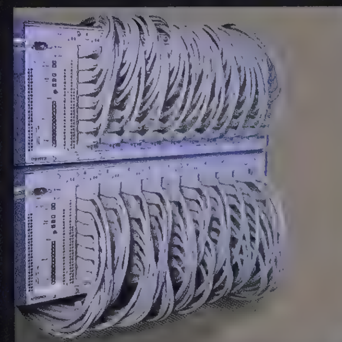


solutions

Pason links the rig site to the office by providing broadband Internet system solutions, including its own proprietary self-aiming satellite dish, that allow the wellsite crew to spend less time on paper work and more time drilling. Over the past several years, the industry has proposed numerous web applications for daily operator reports, contractor equipment inventory and safety reporting systems, approval of expenditures and e-mailing daily drilling programs. If Pason is successful in making reliable broadband Internet connections ubiquitous in the industry, a flood of innovative new drilling management tools will emerge.

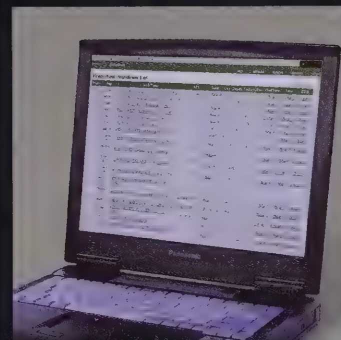
instrumentation and data solutions our customers

Pason's skilled Help Desk answers customer questions on the use of its equipment and software products 24 hours a day, 7 days a week. Pason is committed to maintaining its reputation for industry best service to the wellsite. Pason's field structure is unique to the oilfield service industry in that its field service technicians are based out of their homes, which are located in close proximity to rig sites. To Pason customers, this translates into rapid response times – typically within the hour – compared to traditional service company structures that would require a one way, four to six-hour drive to the site. Each Pason field service technician is on call 24/7 and outfitted with enough equipment for a new system install. In addition to initial equipment installation and setup, field service technicians provide on-site equipment training and maintenance.



need

Customers need reliable, detailed well information. Pason maintains this information along with reports for thousands of wells while employing industry best practices for data storage and security. □ The Pason Internet DataHub provides a convenient and inexpensive mechanism to collect and store financial and drilling engineering data in a true electronic well file. This wellsite data is then disseminated and retrieved by operator partners and service contractors from any location that has Internet access, allowing them to monitor the progress of drilling operations, provide assistance where appropriate and improve overall drilling efficiency.



by bringing the drilling rig to the office.

Pason's skills – robust instrumentation design, field service support, easy to use software, communications and storage infrastructure as well as Help Desk – combine to effectively bring the drilling rig to the office or any location that has Internet access, and as a result, greatly enhance the ability to effectively manage wellsite operations.

Corporate Profile Pason Systems Inc. is the world's largest provider of rental oilfield instrumentation systems that are internally designed and manufactured for use on land-based drilling rigs. Pason offers a tightly integrated package of complex services including data acquisition, wellsite reporting software, remote communications and Internet information management tools.

The Company's strategic focus on unique proprietary solutions and providing the industry best in customer care gives it a competitive advantage in meeting the challenges of the drilling site and bridging the physical separation between the remote rig site and the office. Leveraging these services on its dominant Canadian wellsite presence, a solid position in the United States, and growing operations in Mexico and Argentina, has created strong revenue for Pason as evidenced by its 24% average five-year return on shareholders' equity.

Pason is a Canadian corporation with its head office located in Calgary, and United States offices in Denver and Houston. Common shares of Pason Systems Inc. are listed for trading on the Toronto Stock Exchange under the ticker symbol PSI.

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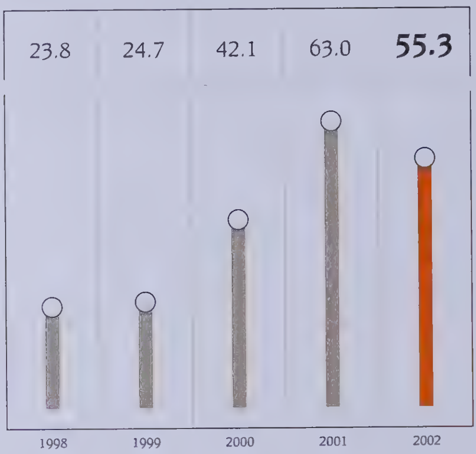
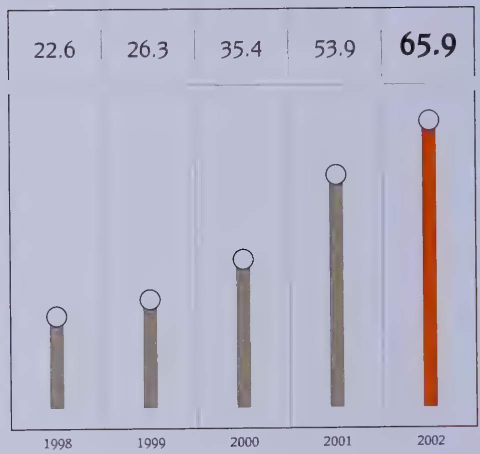
Performance Data

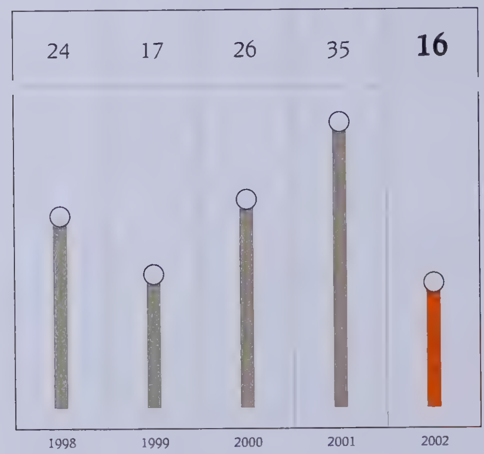
REVENUE ($ MILLIONS)



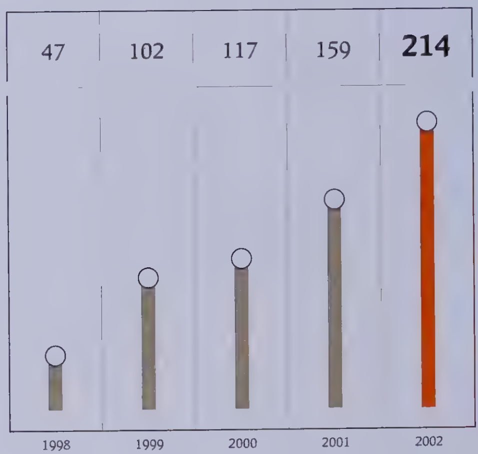
SHAREHOLDERS' EQUITY ($ MILLIONS)



RETURN ON EQUITY (%)



MARKET CAPITALIZATION ($ MILLIONS)



Annual Results

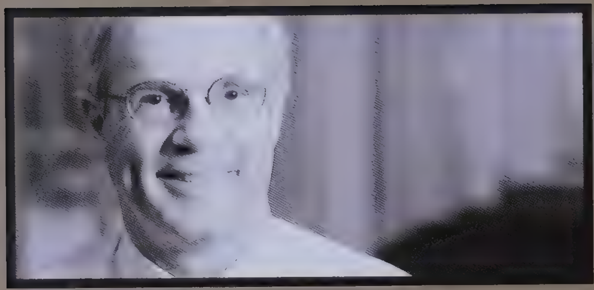
YEARS ENDED DECEMBER 31,	2002	2001	CHANGE
	$	$	%
Revenue	**55,311,000**	63,016,000	(12)
Net earnings	**9,606,000**	15,437,000	(38)
Per share – basic	**0.54**	0.90	(40)
Per share – diluted	**0.53**	0.88	(40)
Cash flow from operations	**18,534,000**	24,941,000	(26)
Per share – basic	**1.04**	1.45	(28)
Per share – diluted	**1.01**	1.42	(29)
Capital expenditures	**14,732,000**	22,921,000	(36)
Working capital	**7,775,000**	5,135,000	51
Total assets	**90,191,000**	82,252,000	10
Shareholders' equity	**65,878,000**	53,941,000	22
Return on shareholders' equity	**16%**	35%	(54)
Market capitalization at year-end	**214,000,000**	159,000,000	35
Weighted average shares outstanding	**17,747,752**	17,147,210	4

For the purposes of cash flow per share calculations, cash flow is defined as "Cash flow from operations" before the change in non-cash working capital.

Quarterly Results

	Q-1	Q-2	Q-3	Q-4
2002	$	$	$	$
Revenue	**16,557,000**	**9,421,000**	**13,720,000**	**15,613,000**
Net earnings	**4,472,000**	**555,000**	**1,680,000**	**2,899,000**
Per share – basic	**0.25**	**0.04**	**0.09**	**0.16**
Cash flow from operations	**7,220,000**	**1,155,000**	**4,209,000**	**5,950,000**
Per share – basic	**0.41**	**0.06**	**0.24**	**0.33**
2001				
Revenue	17,052,000	12,712,000	17,543,000	15,709,000
Net earnings	4,796,000	2,350,000	4,682,000	3,609,000
Per share – basic	0.29	0.13	0.27	0.21
Cash flow from operations	6,620,000	4,354,000	7,130,000	6,837,000
Per share – basic	0.39	0.26	0.41	0.39

For the purposes of cash flow per share calculations, cash flow is defined as "Cash flow from operations" before the change in non-cash working capital.



We are dedicated

The management of drilling operations has always been a challenge because of the physical separation between supervisory personnel located in urban centres and operating personnel situated at remote wellsites. Pason is dedicated to shrinking this geographic gulf by providing a leading edge suite of hardware and software products that facilitate data acquisition and real-time drilling information management.

JIM HILL, PRESIDENT & CHIEF EXECUTIVE OFFICER

Letter to Shareholders

Results for the Year For the first time in its seven years as a public company, Pason was unable to post record revenue. In 2002, revenue fell 12% due primarily to the 24% and 29% year-over-year decline in industry drilling days in Canada and the United States, respectively. Although improved market share and more products per rig site offset much of the waning market conditions, we were unable to fully compensate. Key financial measures for fiscal 2002 were as follows:

- **REVENUE DECREASED 12% TO $55.3 MILLION.**
- **NET EARNINGS DECLINED 38% TO $9.6 MILLION OR $0.54 PER SHARE, STILL THE SECOND BEST ANNUAL RESULTS IN PASON'S HISTORY.**
- **CASH FLOW FELL 26% TO $18.5 MILLION OR $1.04 PER SHARE.**
- **EBITDA WAS DOWN 27% TO $25.7 MILLION OR $1.45 PER SHARE.**
- **SHAREHOLDERS' EQUITY CONTINUED TO GROW A FURTHER 22% TO $65.9 MILLION WITH A 16% RATE OF RETURN.**

Our Business Ten years ago, Pason was simply a small private instrumentation company with two special purpose instruments – pit volume totalizers and remote drilling chokes. Today, Pason has evolved into the world's largest provider of rental oilfield instrumentation. We have developed the tools, both hardware and software, to bring the information age to the drilling rig and to the people who manage these operations from their offices in urban centres. We have established a crucial and valuable role at the wellsite. We provide not only the infrastructure to connect drilling rigs to the "last mile" by permitting Internet access and connection to the downtown office, we also supply the vast majority of "content" or software to capture the wellsite's real-time data and manual reports that must be transferred over this connection back to the office.

The core of our rig presence, Pason's Electronic Drilling Recorder (EDR), now provides data acquisition on over 90% of Canadian rigs, 30% of land rigs in the United States, 20% of land rigs in Mexico, and we recently commenced operations in Argentina. Historically, drilling rig instrumentation was rented within North America and purchased in the rest of the world. Because Pason only rents its equipment and believes this is ultimately the best model for both the provider as well as the customer, the Company has been shut out of many countries. As we move forward, however, more markets are beginning to see the wisdom of the rental model, and as a result, new markets are beginning to emerge for Pason. Such was the case in Argentina where we are now employing the same model that we successfully introduced in Mexico, that of renting our equipment and partnering with a local service company who has been trained in Pason's customer care culture to provide the necessary local service and support.

In late 2002, we began adding broadband Internet communication packages to our EDR base equipment. Widespread use of broadband Internet has previously been hampered by costly labour and transportation charges incurred by specialists who were required to aim the satellite dish at each new well location. Because of the overwhelming need for a reliable, economical, self-aiming alternative, Pason has been working towards a solution on two fronts: its own model as well as sponsoring a third party solution. Since the broadband connection is simply the link between the field data acquisition (EDR) and an Internet site (Pason's DataHub), it is not essential that it be owned by Pason, although a reliable connection solution will benefit Pason with its industry leading position in both EDRs as well as Internet data storage and access.

Pason's Internet DataHub continues to carve out a strong position as the drilling dashboard for rig site personnel. At the peak of this winter's drilling season, the DataHub received and reliably posted close to 30,000 e-mails per day carrying automatic sensor and manual entry data. Our operational excellence in this area has made a strong impression with customers who are now more willing to embrace the concept of Pason expanding the range of collected wellsite data. Also this winter, we rolled out Pason WellView, a daily operations database that layers onto Pason's existing wellsite hardware while requiring no special mobilization by customers, as was required previously. Because data now automatically populates from the daily drilling report to the oil company's daily report, rig personnel save time and office users receive better quality records. Our DataHub has evolved primarily due to the lack of customer consensus and direction as to who was responsible for storing collected data. As Pason continued to fine tune and become more proficient at this service, what was once viewed as an obligation has now become a core strength of our business. As a consequence, we now often win EDR work in the field because of the reliable data storage and retrieval provided by our DataHub.

The development of our WebPay product is ongoing. We are expanding on our model to provide both data collection and transmission infrastructure at the rig and then consolidate the data sources necessary for rig management. We believe this product has tremendous potential and could radically alter the billing and approval process by providing substantial time savings to our customers. Unfortunately, progress has been slow because we are promising much more than the marginal improvement in efficiency of digitizing the current paper payment approval process. The greatest challenge we face with this product is convincing our customers to embrace a radical change, and only by making this major jump will they find the significant efficiency gains they are seeking.

We continue to work on refinements to our current suite of hardware products as well as aggressively investigate and develop new applications. Our Total Gas System has now gained general industry acceptance with approximately 100 rigs currently employing this technology. The Pason Total Gas

System is the only system in the industry that can function reliably without a full time geology specialist on site, which is an extremely important feature in cost conscious markets such as the United States. We expect the growth rate of this system to accelerate significantly during 2003.

Over the past two years, we have been developing an Electronic Auto Driller used to maintain a constant weight on the drill bit or rate of penetration while drilling. We experienced some setbacks in 2002 due to design limitations detected in certain sub components that were not actually built by Pason. This required our engineers to make compensating design changes, and although we have solved these problems, it has delayed moving the Auto Driller into our regular operations group for performance testing. We expect to see revenue from this new product later in the year.

Internally, we continue to measure our performance by how much rental product revenue we generate for each drilling day logged in the industry. Improvements in market share, prices or the addition of new products all positively affect this number while price decreases obviously hurt this metric. In Canada, our revenue increased 17% to $349 per industry drilling day. As you may recall, in my March 20, 2001 annual Letter to Shareholders I stated that we could see the potential of generating an economic package in excess of $700 per drilling day. I am pleased to report that in fact we have already achieved over $800 a day on a number of rigs in Canada. This would seem to prove our assertion that we can continue to add value and revenue to each wellsite. In the United States, although unit prices dropped 21% due to extremely competitive market conditions that are encountered in any year of depressed drilling activity, we did however, increase our revenue to $64 per industry drilling day, a 31% improvement over 2001.

Outlook

Oil and gas prices have remained strong for the past half-year, which presents the potential for our customers to substantially increase their drilling expenditures and activities as a result of higher cash flows. Winter drilling activity in Canada was much stronger than the previous year, but it remains to be seen whether this year-over-year improvement continues into the summer. In the United States, it has only been within the past several months that the rig count has climbed above the prior year's levels. While most of our customers have been quite candid about their 2003 drilling plans, the plummeting gas storage levels indicate that gas prices should remain high, and as a result, will encourage much needed gas drilling.

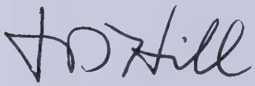
As our Company did during the 1998/1999 drilling slowdown, we have used the extra down time to strengthen our organization and prepare for the next surge in activity. In the last boom, an independent evaluation of Pason would have said that our fortunes were carried by our hardware product expertise and that software development played a minor role. Over the past year, however, we have

developed sophisticated new software and project management skills that have allowed us to move our key EDR product to a new Linux platform and thereby facilitating faster deployment of new customer-requested software features.

Our strengths in hardware design, software development, service support, data communications and storage infrastructure present formidable barriers to competitors in our industry and I believe these skills will allow Pason to continue to outperform the general industry, and as a result, continue to offer superior returns for our shareholders going forward.

I would like to thank all of our employees and board members for their continued effort and commitment in helping to execute Pason's vision.

On behalf of the Board of Directors,



JIM HILL
PRESIDENT & CHIEF EXECUTIVE OFFICER

March 14, 2003

Management's Discussion and Analysis

The following discussion and analysis has been prepared by management and is a review of the financial results of the Company based on accounting principles generally accepted in Canada. Its focus is primarily a comparison of the financial performance for the years ended December 31, 2002 and 2001 and should be read in conjunction with the consolidated financial statements and accompanying notes.

Certain information regarding the Company contained herein may constitute forward-looking statements under applicable securities laws. Such statements are subject to known or unknown risks and uncertainties that may cause actual results to differ materially from those anticipated or implied in the forward-looking statements.

YEARS ENDED DECEMBER 31,	2002	2001	CHANGE
	$	$	%
REVENUE			
Drilling recorder rentals	**27,730,000**	31,796,000	(13)
Pit volume totalizer rentals	**16,149,000**	17,317,000	(7)
Geological services	**5,616,000**	9,404,000	(40)
Total gas rentals	**2,199,000**	1,105,000	99
Choke control rentals	**1,416,000**	1,292,000	10
Mobilization income	**2,201,000**	2,102,000	5
Total revenue	**55,311,000**	63,016,000	(12)
EXPENSES			
Rental services	**17,088,000**	13,641,000	25
Geological services	**4,608,000**	6,262,000	(26)
Shop	**2,359,000**	2,551,000	(8)
Research and development	**3,009,000**	2,750,000	9
Administration	**2,498,000**	2,415,000	3
Interest	**1,107,000**	1,324,000	(16)
Depreciation and amortization	**8,913,000**	7,341,000	21
Consolidated total expenses	**39,582,000**	36,284,000	9
Net earnings (after taxes)	**9,606,000**	15,437,000	(38)
Per share – basic	**0.54**	0.90	(40)
Cash flow from operations	**18,534,000**	24,941,000	(26)
Per share – basic	**1.04**	1.45	(28)
Margins			
Rental services	**66%**	75%	(12)
Geological services	**18%**	33%	(45)

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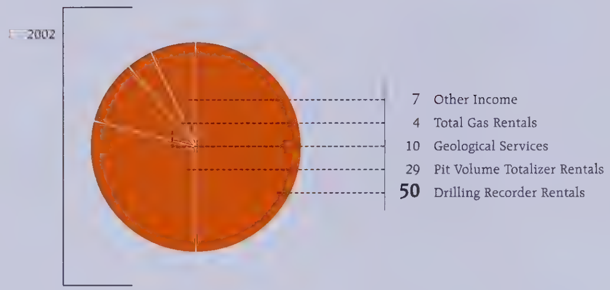


Pason derives its revenue from the rental of instrumentation and data services to oil and gas companies and drilling contractors throughout Canada, the United States, Mexico and Argentina. After experiencing extraordinary operating results in its first six years as a public company, 2002 was met with a decline in revenue, margin and profit. Many accumulating factors were responsible for these financial results, the most significant being a weak economy, unstable commodity prices and the ensuing downturn in oil and gas drilling activity. However, Pason recognized the opportunities that are created in a volatile market and continued to aggressively pursue its strategy: to grow through increased market share and provide more products per rig site.

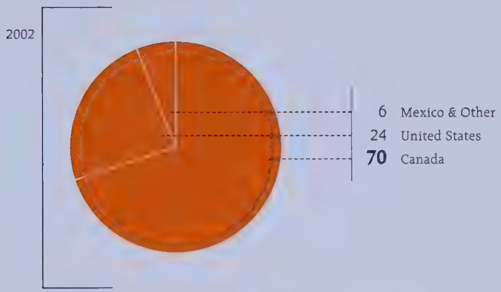
Revenue

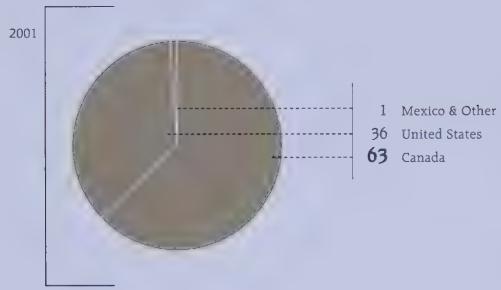
Revenue, generated primarily from instrumentation rentals and geological services, fell to $55.3 million from $63.0 million recorded in 2001. This 12% decline was due to decreases in the number of Canadian and U.S. industry drilling days (24% and 29%, respectively) as well as a 21% reduction in U.S. unit prices. The decline was less than the reduction in drilling days because the decrease was partially offset by new product growth.

INSTRUMENTATION RENTALS

Pason is the world's largest provider of rental oilfield instrumentation systems that are internally designed and manufactured for use on land-based drilling rigs. The Company delivers an integrated package of rental products that offer wellsite data acquisition and drilling management benefits at both the rig site and in the office. During 2002, revenue generated by instrumentation rentals totaled $49.7 million compared to $53.6 million a year ago. Canadian rentals revenue dropped 11% to $32.1 million, rentals revenue generated from U.S. operations decreased 5% to $16.4 million from $17.3 million, while revenue from Mexico and other international activities increased 211% to $1.2

SEGMENT OPERATING PROFIT (%)



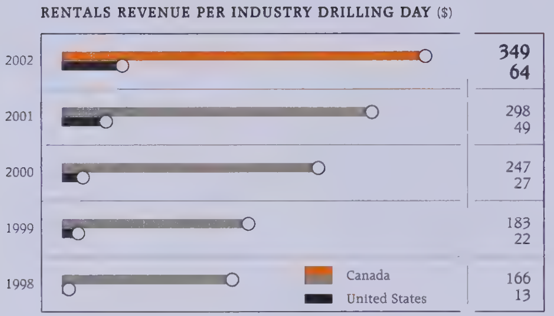


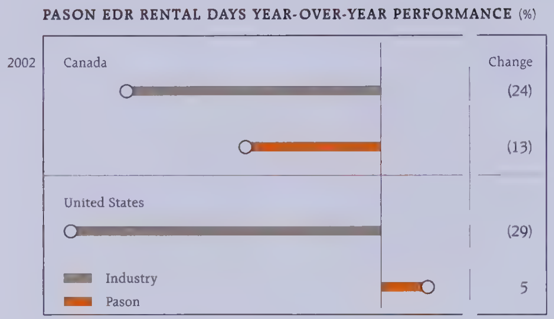
million. The gross margin (rentals revenue less rental expenses) as a percentage of revenue was 66% compared to 75% in 2001.

The development of the Company's Canadian and U.S. rentals revenue per industry drilling day is outlined below:

	INDUSTRY DRILLING DAYS	PASON RENTALS REVENUE	REVENUE PER DAY
	#	CDN$	CDN$
CANADA*			
1998	89,400	14,800,000	166
1999	81,800	15,000,000	183
2000	117,400	29,000,000	247
2001	120,400	35,900,000	298
2002	**92,000**	**32,088,000**	**349**
UNITED STATES			
1998	258,400	3,300,000	13
1999	191,600	4,200,000	22
2000	281,400	7,500,000	27
2001	354,400	17,300,000	49
2002	**253,700**	**16,276,000**	**64**

* Source: Canadian Association of Oilwell Drilling Contractors.



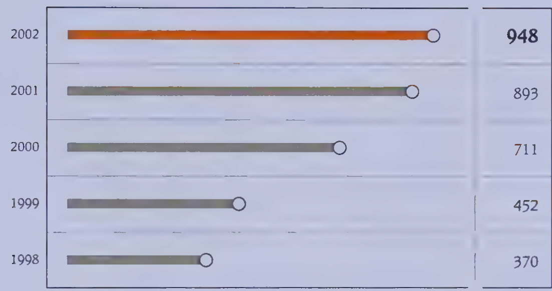


Pason anticipates that the daily rental value of its current data acquisition, control and data management products as well as those in development could generate an economic package in excess of $700 per drilling day in Canada, with the potential for continued growth in this market despite its significant EDR market share. As noted earlier in this report, Pason has already achieved over $800 a day in products on a number of Canadian rigs. The progress made over the past five years in Canada indicates that the Company is well on its way to consistently achieving its daily rental value goal.

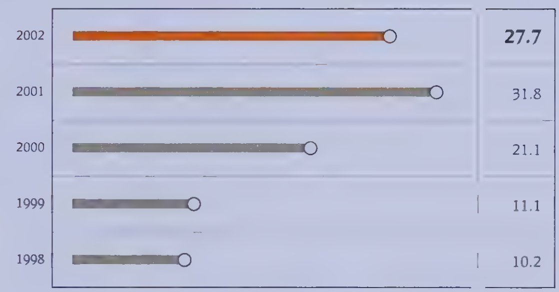
ELECTRONIC DRILLING RECORDERS

The Electronic Drilling Recorder (EDR) serves as the core of the Company's rig presence. Pason's EDR is a complete system of instrumentation and monitoring equipment, which acts as a base for all data capture, data display and communications at the drilling wellsite, that is configured as required. During 2002, the Company met all requests for its EDR and, given the slump in drilling activity experienced throughout most of the year, initiated a corresponding reduction in new EDR builds from 182 units in 2001 to 56 units in 2002. At year-end, Pason's electronic data acquisition instrumentation had been installed on over 90% of all Canadian rigs and was on 30% of all active U.S. land rigs, thereby generating revenue of $27.7 million compared to $31.8 million recorded in 2001. The year-over-year revenue decrease was primarily due to a 13% drop in Pason Canadian rental days to roughly 84,000 from 96,000 in 2001. In the United States, Pason rental days increased 5% to 61,000 from 58,000 a year ago. The Company continues to invest heavily in upgrading its EDR fleet with all of the features its customers require. During the first six months of 2002, network speed at the rig was improved significantly, and as a result, the Company is currently enhancing its software to allow its EDRs to take advantage of the broadband Internet access expected to be economically viable and available at most wellsites by the end of 2003. Pason is looking to significantly increase its EDR market presence in the United States over the next 12 months.

EDR SYSTEMS (SYSTEMS AT YEAR-END)



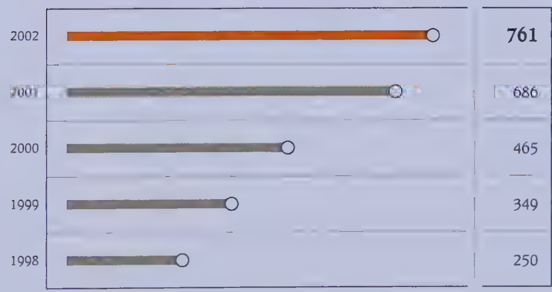
EDR REVENUE ($ MILLIONS)



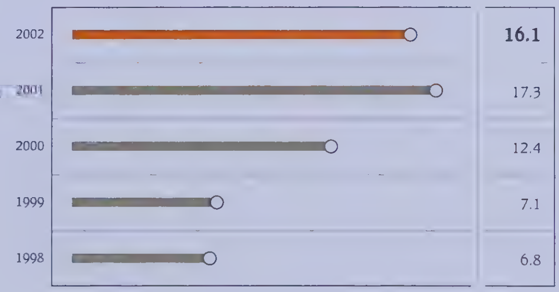
PIT VOLUME TOTALIZERS

The Pit Volume Totalizer (PVT) is Pason's proprietary solution for the detection and early warning of "kicks" that are caused by hydrocarbons entering the wellbore under high pressure and expanding as they migrate to the surface. At year-end, the Company's PVT had been installed on over 80% of Canadian and 60% of U.S. rigs operating with a Pason EDR system. A decrease in Canadian PVT rental days contributed to a 7% decline in rentals revenue from $17.3 million a year ago to $16.1 million in 2002. The Company's PVT rental days in Canada were down 11% to 73,000 from 82,000 in 2001 while in the United States, rentals were up 3% to 35,000 compared to 34,000 the prior year. Canadian drilling regulations now allow operators to reduce surface casing depth when a PVT is employed, thereby justifying the use of this instrument on practically every well.

PVT SYSTEMS (SYSTEMS AT YEAR-END)



PVT REVENUE ($ MILLIONS)



TOTAL GAS SYSTEMS

The Pason Total Gas System (TGAS) measures the total hydrocarbon gases (C1 through C5) exiting the wellbore and then calculates the lag time to show the formation depth where the gases were produced. The complex system, which was introduced to the marketplace in early 2001, seeks to provide a more accurate gas sample while dramatically reducing daily maintenance requirements. As the Company rolled out a larger fleet of systems in 2001, several design flaws were detected and subsequently rectified, however slowing acceptance. Another obstacle encountered was marketing related. Despite the fact that drilling personnel, Pason's traditional customer base, were solidly behind the use of Pason's TGAS, the same could not be said for wellsite geologists with whom Pason had had little previous contact. Through a concentrated marketing effort, however, Pason has been gaining greater acceptance from this new customer group and still believes that its TGAS will dominate the industry. Revenue generated from this product doubled in 2002 to total $2.2 million compared to $1.1 million recorded the prior year. Although these results were below Company expectations, they were significantly improved over 2001 and further growth acceleration is expected in 2003. Currently, Pason's TGAS has the potential for use on 75% of Canadian rigs and 50% of U.S. rigs.

CHOKE CONTROL SYSTEMS

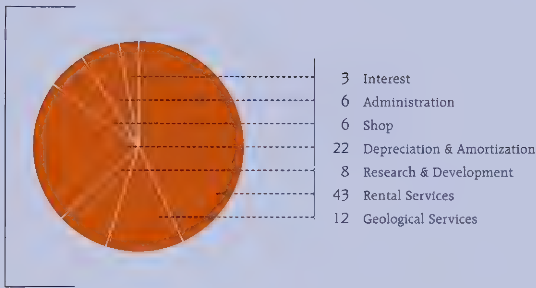
Pason's Electronic Choke Control System is used to control and remove detected gas "kicks" from the wellbore. During 2002, revenue from this product was up 10% to $1.4 million from $1.3 million a year ago. This system has been installed on approximately 25% of all Canadian rigs in operation. Pason is again pushing a new business model where the choke valve portion of the system becomes the responsibility of the drilling contractor while Pason provides only the electronic actuation and display. Although this model provides greater industry safety, it has yet to gain acceptance in the United States and, therefore, to date the majority of revenue for this product has been derived from Canada, and more recently Mexico. The Company still expects to eventually generate increased revenue from its Choke Control System in the United States.

GEOLOGICAL SERVICES

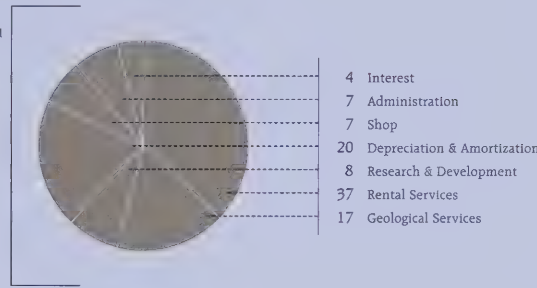
In the United States, Pason provides skilled wellsite geologists and mudlogging technicians to monitor gas in the drilling returns, to pick formation tops and to analyze drilling cuttings. This service is offered only in the U.S. market because of the strong link between the geological service provider and the specialized equipment that is employed. Through Pason's unique suite of integrated instrumentation products, the Company can assist customers in an environment of scarce geological talent as well as provide significant cost savings with supervision of multiple wells. Despite the fact that year-over-year revenue generated from geological services was down 40% from $9.4 million to $5.6 million, Pason has not lost market share. The gross margin for these services was 18%, down from 33% in 2001. To date, Pason's geological services remain concentrated in the U.S. Rocky Mountains

EXPENSES (%)

2002



2001



where there is a shortage of pipeline capacity to export natural gas from the region. This resulted in a more pronounced slowdown in drilling in this region versus the industry at large. The low prices and lack of activity that have resulted from the insufficient pipeline capacity should be alleviated by the summer of 2003.

Expenses

Expenses incurred by the Company over the past several years have reflected the cost associated with building and maintaining a field service infrastructure to accommodate the higher activity levels experienced in 2000, the first nine months of 2001, and originally expected for the last half of 2002. Accordingly, consolidated total expenses rose 9% to $39.6 million in 2002 from $36.3 million the prior year.

During 2002, rental services expenses, which represented 43% of total expenses, increased 25% or $3.5 million to $17.1 million compared to $13.6 million in 2001. These expenses consisted primarily of wages and related benefit costs, which represent approximately 47% of the total rental services expenses in both Canada and the United States, and the additional direct costs of field servicemen, including but not limited to vehicle costs, communication, equipment repairs and freight. Of the $3.5 million increase in total rental services expenses, $2.7 million was incurred in the United States, of which $1.2 million was for labour and related costs, $0.8 million for vehicle and communication costs, $0.3 million for equipment repairs and the remaining $0.4 million for other expense items. The $0.8 million increase in Canadian rental services expenses was spread evenly across labour and related costs, equipment repairs, vehicle costs and communication. As industry activities were expected to increase in the last half of 2002 and in order to maintain strong levels of service, the Company continued to recruit and train additional field technicians as required. Pason's field technicians are

employed full time and year round, and as a result, the Company's related expenses have a heavily weighted, fixed component that is critical to its high service level. At December 31, 2002, there were 80 field service technicians versus 66 at December 31, 2001, a significant contributor to the increase in overall rental services expenses, especially in the United States. During the year, Pason added U.S. field service technicians who assisted in growing the Company's market share and volume, but as a result, put additional pressure on the Company's margins.

Geological services expenses decreased 26% from $6.3 million to $4.6 million due primarily to labour and related costs, which represent over 85% of the total of these expenses compared to 75% in 2001. This is the area where the expenses are more variable weighted than the rest of the Company.

Costs related to the assembly and distribution of Pason products, which make up shop expenses, declined 8% from $2.6 million to $2.4 million. Over 40% of the decrease was due to lower personnel costs as less temporary employees were used. The remaining decrease attributed to lower freight and shipping costs.

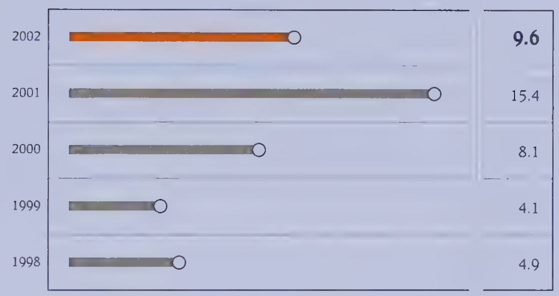
Research and development expenses, largely labour and occupancy related, increased 9% to $3.0 million from $2.8 million a year ago while capitalized deferred development also increased 8% from $1.3 million in 2001 to $1.4 million in 2002. The year's total increase in R&D, expensed and capitalized, was $0.4 million or 10% compared to $0.3 million or 8% a year ago. Labour and related costs accounted for the majority of the increase in expensed and capitalized deferred development. The current level of R&D expenses should be maintained into 2003.

Administrative expenses increased 3% to $2.5 million from $2.4 million in 2001 with no notable expense contributing to this nominal year-over-year increase. The level of administrative expenses is expected to remain relatively constant in 2003.

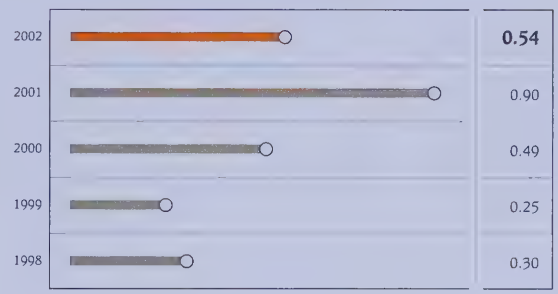
Interest expense decreased 16% from $1.3 million to $1.1 million. The Company continued to use its credit facilities as required in both Canada and the U.S., however in a period of slow drilling activity, Pason's largely discretionary capital expenditures are reduced resulting in less use of its lines of credit. During 2003, the use of lines of credit is expected to be high given the increased levels of drilling activity and demand for products. However, the Company continues to pay down its lease obligations, which in turn decreases the associated interest expense.

Depreciation and amortization expenses increased 21% to $8.9 million from $7.3 million in 2001, representing 22% of the year's total expenses versus 20% a year ago. A significant portion of the Company's tangible assets are depreciated using a unit-of-use method of accounting as it best matches revenue and expenses. As a consequence, Pason should have seen these expenses decrease during 2002, but in fact, a $2.1 million increase in depreciation was actually recorded as a result of changes in accounting estimates. Effective January and July 2002, changes to certain useful lives

NET EARNINGS ($ MILLIONS)



NET EARNINGS PER SHARE ($ BASIC)



were made based on management's observations as to equipment wear and tear and obsolescence. More specifically, the number of EDR rental days for the unit-of-use method was changed from 1,800 to 1,575; likewise, the drilling choke control was changed from 20% declining-balance to the unit-of-use method and to 1,800 rental days. As at July 1, 2002, satellite telephones, which were previously depreciated as part of the EDRs, were reclassified to their own category and subsequently depreciated on a straight-line basis over 30 months instead of 1,575 rental days.

Current income tax expense fell 33% from $9.1 million in 2001 to $6.1 million in 2002. Lower earnings before tax of $15.7 million, down 41% from 2001, attributed to a decrease in current taxes payable consistent with a decrease in earnings before tax. The Company's current and future tax rate for 2002 was 38.9% versus 42.3% for 2001. As federal and provincial tax rates are expected to drop over the upcoming year, Pason will see the benefit in lower current and future tax.

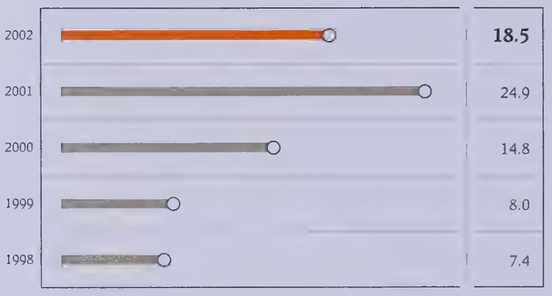
Net Earnings

Net earnings decreased from $15.4 million or $0.90 per share basic in 2001 to $9.6 million or $0.54 per share basic in 2002. This 38% earnings contraction was due primarily to decreases in the Company's revenue and margins.

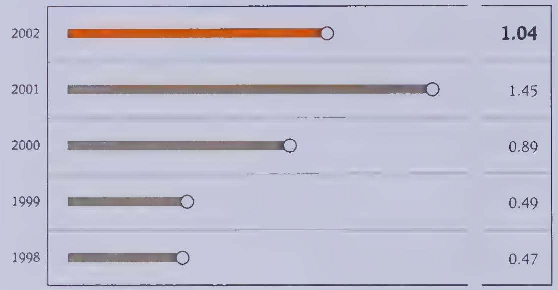
Cash Flow from Operations

Operating cash flow fell 26% to $18.5 million or $1.04 per share basic in 2002 from $24.9 million or $1.45 per share basic a year ago. The majority of this cash flow decline is a result of the $5.8 million decrease in earnings, an increase in non-cash depreciation totaling $1.6 million and a decrease in future income tax of $2.1 million. During 2002, cash flow was used primarily to finance the Company's reduced capital expenditures program and improve its year-end working capital position from $5.1 million to $7.8 million.

CASH FLOW ($ MILLIONS)



CASH FLOW PER SHARE ($ BASIC)



Margins

In 2002, the margin generated by the Company's rental products dropped from 75% to 66%. The ramp up in rental services infrastructure during the last three years positioned Pason to benefit from the strong industry activity experienced in 2001 and that is expected again in 2003. The Company, unlike many other service providers, improves its margins not from increased prices, but from an increased number of rental products per site and increased market share or volume.

Despite concerted efforts to manage the costs of providing geological services, assisted in part by the new integrated model that includes the TGAS system, the 2002 geological services margin fell to 18% from 33% a year ago.

Liquidity and Capital Resources

The Company's internal sources of liquidity are cash and cash flow from operations. External sources include the unutilized portion of revolving credit facilities and equipment financings by way of capital leases.

At December 31, 2002, the Company's working capital position was $7.8 million versus $5.1 million at year-end 2001. This 51% improvement allows for greater financial flexibility in the current uncertain economic environment.

Proceeds from the exercise of Company stock options totaled $2.5 million compared to $1.8 million in 2001, resulting in the issuance of 467,242 common shares versus 663,843 common shares the prior year. The average per share exercise price doubled from $2.71 in 2001 to $5.41 in 2002.

During 2002, cash flow funded the Company's entire $14.7 million capital expenditures program, representing a 36% or $8.2 million decrease from the prior year's total expenditures amount of $22.9 million. Funds were used to acquire and build $13.3 million of new capital assets and for

product enhancements, with a further $1.4 million spent on deferred development costs versus $21.6 million and $1.3 million, respectively, in 2001. Geographically, $8.7 million of the new capital assets were in Canada, $4.0 million in the U.S. and $0.6 million in Mexico. This compares to $10.9 million, $10.1 million and $0.6 million, respectively, a year ago. Given the weakness in commodity prices and the lower level of drilling activity expected in the first half of 2002, a slow down on capital expenditures was initiated for the 2001 fourth quarter and remained restricted until the last quarter of 2002. Capital expenditures for 2003 are expected to ramp up as drilling activity increases.

At December 31, 2002, long-term capital lease obligations amounted to $3.0 million, representing 0.16 times 2002 cash flow compared to 0.26 times a year ago.

The Company's maximum operating line of credit is $5.0 million in Canada and US$1.5 million in the United States. At December 31, 2002, $3.4 million and US$1.0 million, respectively, were drawn on these facilities with $1.6 million and US$0.5 million available for use.

New Products

Through its rental products, Pason continues to add value to the data acquired at the wellsite. The Company's vision is to converge all drilling engineering and financial wellsite data together on one Internet site. This site will provide internally developed management tools with broad market appeal plus facilities to download data into more narrowly focused third party specialty applications.

INTERNET DATAHUB

Pason's Internet DataHub has been in place since 1999. It was initially designed to simply collect data from the rig and act as an incentive to use other Pason products for wellsite data acquisition. That vision, however, has evolved to the point where the DataHub now provides a platform for several new services that are being marketed to the community of industry users who regularly visit the Pason DataHub site. As broadband Internet access to the rigs became more common late in 2002, the DataHub became even more critical as it blends both historical and real-time data access. There are currently almost 2,900 registered users of the Pason Internet DataHub versus 2,000 a year ago.

PASON WELLVIEW

In addition to sensor data collected by Pason, there is a considerable amount of manual data that must be collected daily by wellsite supervisors. Pason has been carefully considering this problem, and in late 2002 rolled out Pason WellView, a solution to the existing inherent compatibility and mobilization challenges. Building on the wellsite engineering package developed by Peloton Computer Enterprises, a leading provider of this type of product, Pason WellView provides a generic engineering database capture module as part of the Pason EDR software package. This new module follows the

Pason EDR and the rigs on which it works. As a result, wellsite supervisors are more familiar with how to use the software while drilling superintendents in the office no longer need to make special mobilization efforts for software and communications. Pason displays all data in standard forms on its Internet DataHub, although if customers require greater analysis or desire to have the information transferred to another supplier's database, data is available for export from the Pason DataHub using WITSML.

WEBPAY

For the past three years Pason has been developing WebPay, a solution for the challenges faced in gathering, approving and processing charges generated at remote rig sites. The Company has been working primarily with a U.S. drilling contractor and the benefits from the system's automatic charge creation, rapid approval and the complete absence of paper have already been achieved. Pason expects to have the product ready for use in limited circumstances by the middle of 2003.

AUTO DRILLER

Over the past two years, Pason has been developing an Electronic Auto Driller used to maintain a constant weight on the drill bit or rate of penetration while drilling. The Company experienced some setbacks in 2002 due to design limitations detected in certain sub components that were not actually built by Pason. Although the Company has solved these problems, it has delayed moving the Auto Driller into its regular operations group for performance testing. Pason expects to see revenue from this new product later in the year.

New Markets

Several years ago, Pason developed a new international business model for renting its equipment in countries where drilling rig instrumentation has typically been purchased. Pason rents its equipment package that can include an EDR, PVT and TGAS for each rig, and then partners with a local service provider who has been trained in Pason's service culture to supply the necessary local service and support. As a result, Pason retains ownership of its equipment while protecting it from unexpected costs associated with local service companies.

Pason's first serious international operation employing this model commenced in Mexico in May 2001 whereby the Company provided five rig instrumentation packages while service activities were provided by a local Mexican company. Over the past two years, increased activity levels and strong customer satisfaction in that country have led to increased opportunities for Pason. During 2002, operations from this market contributed $1.2 million to the Company's total rentals revenue. Pason currently provides instrumentation packages for 13 rigs in Mexico.

Through the success of this business model, Pason recently expanded its operations into the Argentina market. Pason will continue to investigate new markets as justified by opportunity and demand.

Business Risks

Pason derives its revenue from the rental of instrumentation and data services to oil and gas companies and drilling contractors throughout Canada, the United States, Mexico and Argentina. As a result, the major area of uncertainty for Pason is that the demand for its services is directly related to the strength of its customers' capital expenditures programs. The level of capital programs is strongly affected by the level and stability of commodity prices, which can be extremely difficult to predict and beyond the control of Pason and its customers. During periods of uncertainty, oil and gas companies tend to bias their capital decisions on conservative outlooks for commodity prices. The creation of royalty trusts with limited drilling activity, the large capital-intensive oil sands projects and expanding international activities by many energy companies all influence the level of capital expenditures in Canada, in particular.

Weakness in commodity prices could also impact the ability of the Company's customers to pay for the services provided. However, as Pason has a very broad customer base and its services are a minor component when looking at the overall cost of drilling a well, the risk is minimal.

In late 2002, the Government of Canada ratified the Kyoto Protocol. Details of its implementation and associated costs have yet to be determined, and as a result, the effect on customers' cash flow and capital expenditures programs remain uncertain.

Merger and acquisition activity in the oil and gas exploration and production sector may impact demand for the Company's services, as customers tend to focus on reorganization activities prior to committing funds to major drilling programs.

In addition to the cyclical nature of its business, Pason is also subject to risks and uncertainties associated with weather and seasonality. Pason continues to react to unfavourable weather conditions and spring breakup, which limit well access in Canada, through diversification into geographic regions such as the United States, Mexico and Argentina where these factors are less likely to influence activity.

The Company does not employ hazardous materials, so the possibility of environmental liabilities is limited.

Pason carries adequate levels of insurance to protect the Company. Due to the wide geographical distribution of equipment, the possibility of a loss to a significant portion of its asset base is extremely unlikely. As the Company's equipment is largely unmanned, the customer assumes responsibility for its operation.

Outlook As commodity price uncertainty and threats of war continue, concern exists with the supply and demand fundamentals for crude oil and natural gas. Throughout the latter half of 2001 and through most of 2002, low gas prices and a weak economy put pressure on the industry to maintain reduced drilling activity levels. As a result of this pressure, 2002 was a year of slow activity with only about 14,500 wells drilled in 92,000 drilling days in Canada versus fewer than 18,000 wells in 120,400 drilling days in 2001. Drilling activity for 2003, as forecast by the drilling industry, is expected to again reach close to 18,000 wells with approximately 117,500 drilling days. Pason continues to be well positioned to profit from the high levels of oilfield activity and increased market share. The Company expects to spend in excess of $15.0 million during 2003 to add new products, new units of existing products and enhancements in Canada, and to a greater extent in the United States, Mexico and Argentina where significant room for additional market share exists. The Company will continue to pursue additional international opportunities that fall within its service model parameters.

Pason invested significantly to put in place an infrastructure that supported the oil and gas industry's 2001 activity levels, levels that are expected to be reached or surpassed in 2003. The Company wants to ensure it is not limited by a shortage of trained workers, and therefore continues to maintain permanent full time field service technicians throughout the year. During a challenging 2002, the Company's focus was to maximize the relationship between operating efficiencies, operating costs and customer service, and this focus will also continue in 2003, in what is anticipated to be a much improved environment.

Management's Report

To the Shareholders of Pason Systems Inc.

The accompanying consolidated financial statements are the responsibility of management and have been approved by the Board of Directors of the Company. Management is responsible for and has prepared and presented the consolidated financial statements in accordance with Canadian generally accepted accounting principles and has made significant accounting judgements and estimates as required. Management has ensured that financial information contained elsewhere in this Annual Report is consistent with the consolidated financial statements.

The Board of Directors is responsible for reviewing and approving the consolidated financial statements and ensuring management meets their financial reporting responsibilities.

JIM HILL
PRESIDENT & CHIEF EXECUTIVE OFFICER

JOANNE DICKIE
CHIEF FINANCIAL OFFICER

Calgary, Alberta
March 10, 2003

Auditors' Report

To the Shareholders of Pason Systems Inc.

We have audited the consolidated balance sheets of Pason Systems Inc. as at December 31, 2002 and 2001 and the consolidated statements of earnings and retained earnings and of cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2002 and 2001 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Deloitte & Touche LLP

CHARTERED ACCOUNTANTS

Calgary, Alberta
February 21, 2003

Consolidated Balance Sheets

DECEMBER 31,	2002	2001
	$	$
ASSETS		
Current		
Cash and term deposits	**676,995**	1,253,713
Accounts receivable	**16,503,650**	14,986,321
Income taxes receivable	**1,630,962**	–
Inventory	**3,480,100**	3,592,319
Prepaid expenses	**435,812**	443,256
	22,727,519	20,275,609
Capital assets (NOTE 6)	**64,153,095**	59,156,373
Deferred development costs (NOTE 7)	**3,310,157**	2,820,290
	90,190,771	82,252,272
LIABILITIES		
Current		
Bank indebtedness (NOTE 8)	**4,994,442**	2,610,000
Accounts payable and accrued liabilities	**6,301,521**	6,192,477
Income taxes payable	**–**	2,840,873
Current portion of long-term debt (NOTE 9)	**275,148**	278,525
Current portion of obligations under capital leases (NOTE 10)	**3,380,966**	3,219,003
	14,952,077	15,140,878
Long-term debt (NOTE 9)	**114,594**	394,527
Obligations under capital leases (NOTE 10)	**2,977,768**	6,491,392
Future income taxes (NOTE 12)	**6,268,049**	6,284,059
	24,312,488	28,310,856
SHAREHOLDERS' EQUITY		
Share capital (NOTE 11)	**16,574,608**	14,045,635
Foreign currency translation adjustment	**1,906,588**	2,105,033
Retained earnings	**47,397,087**	37,790,748
	65,878,283	53,941,416
	90,190,771	82,252,272

Approved by the Board of Directors

HAROLD R. ALLSOPP
DIRECTOR

JAMES B. HOWE
DIRECTOR

Consolidated Statements of Earnings and Retained Earnings

YEARS ENDED DECEMBER 31,	2002	2001
	$	$
REVENUE		
Drilling recorder rentals	**27,729,596**	31,795,631
Pit volume totalizer rentals	**16,148,493**	17,316,714
Geological services	**5,616,228**	9,403,774
Total gas rentals	**2,199,464**	1,105,317
Choke control rentals	**1,415,865**	1,292,090
Mobilization income	**2,201,349**	2,102,598
	55,310,995	63,016,124
EXPENSES		
Rental services	**17,087,632**	13,641,302
Geological services	**4,608,430**	6,261,824
Shop	**2,358,718**	2,551,586
Research and development	**3,008,520**	2,750,333
Administration	**2,498,016**	2,414,706
Interest on long-term obligations	**762,420**	1,075,672
Interest – other	**345,775**	248,011
Depreciation and amortization	**8,912,837**	7,341,047
	39,582,348	36,284,481
Earnings from operations before income taxes	**15,728,647**	26,731,643
INCOME TAXES (NOTE 12)		
Current	**6,107,492**	9,131,759
Future	**14,816**	2,162,597
	6,122,308	11,294,356
Net earnings	**9,606,339**	15,437,287
Retained earnings, beginning of year	**37,790,748**	22,449,369
Repurchase of common shares (NOTE 11(B))	**–**	(95,908)
Retained earnings, end of year	**47,397,087**	37,790,748
Earnings per share (NOTE 14)		
Basic	**0.54**	0.90
Diluted	**0.53**	0.88

Consolidated Statements of Cash Flows

YEARS ENDED DECEMBER 31,	2002	2001
	$	$
Cash flows related to the following activities:		
OPERATING		
Net earnings	9,606,339	15,437,287
Adjustments for:		
Depreciation and amortization	8,912,837	7,341,047
Future income taxes	14,816	2,162,597
Cash flow from operations	18,533,992	24,940,931
Changes in non-cash working capital	(5,760,457)	(4,849,399)
	12,773,535	20,091,532
FINANCING		
Issue of common shares under the employee stock option plan	2,528,973	1,797,421
Repurchase of common shares under Normal Course Issuer Bid (NOTE 11(B))	–	(114,220)
Repayment of long-term debt	(283,310)	(224,294)
Repayment of capital leases	(3,351,661)	(1,436,078)
	(1,105,998)	22,829
INVESTING		
Purchase of capital assets	(12,668,615)	(20,625,198)
Development costs	(1,400,649)	(1,331,864)
Proceeds on disposal of capital assets	300,960	226,785
Change in non-cash working capital	(661,948)	(964,431)
	(14,430,252)	(22,694,708)
Foreign currency translation adjustment	(198,445)	1,372,634
Net (decrease) increase in cash and cash equivalents	(2,961,160)	(1,207,713)
Cash and cash equivalents, beginning of year	(1,356,287)	(148,574)
Cash and cash equivalents, end of year	(4,317,447)	(1,356,287)
Represented by:		
Cash and term deposits	676,995	1,253,713
Bank indebtedness	(4,994,442)	(2,610,000)
	(4,317,447)	(1,356,287)

Supplemental cash flow information (NOTE 16)

Notes to Consolidated Financial Statements

YEARS ENDED DECEMBER 31, 2002 AND 2001

1. DESCRIPTION OF BUSINESS

Pason Systems Inc. (the "Company") designs and manufactures for rent, specialized proprietary instrumentation for use on land-based drilling rigs.

2. BASIS OF PRESENTATION

The accompanying consolidated financial statements include the accounts of Pason Systems Inc. and its wholly owned subsidiaries Pason Systems Corp., Pason US Holdings Corp., Pason de Mexico S.A. de C.V. and Pason Systems USA Corp, a wholly-owned subsidiary of Pason US Holdings Corp.

Certain comparative figures have been reclassified to conform to the current year presentation.

3. CHANGE IN ACCOUNTING POLICIES

The Company adopted a new accounting recommendation of the Canadian Institute of Chartered Accountants on goodwill and other intangible assets, and as a result, the Company stopped amortizing goodwill that was acquired prior to July 31, 2002, effective January 1, 2002. Under the new standard, all goodwill and other intangible assets with indefinite lives that are currently included in capital assets in the Company's consolidated balance sheet will no longer be amortized to income over time and will be subject to a periodic impairment review to ensure that the fair value remains greater than, or equal to, book value. Any excess of book value over fair value will be charged to income in the period in which the impairment is determined.

Effective January 1, 2002, the Company adopted a new accounting recommendation for Stock-Based Compensation, which establishes the standards for recognition, measurement and disclosure of stock-based compensation and other stock-based payments made in exchange for goods and services provided by employees and non-employees. The standard requires that a fair value based method of accounting be applied to all stock-based payments to non-employees and to employee awards of stock, that call for settlement in cash or other assets or are stock appreciation rights that call for settlement by issuance of equity instruments. The new standard permits the Company to continue to follow its existing policy of recording no compensation costs on the grant of stock options to employees. No restatement of prior periods was required as a result of the adoption of the new standard.

4. CHANGE IN ACCOUNTING ESTIMATES

The electronic drilling recorders are recorded at cost and prior to January 1, 2002 had been depreciated using a unit-of use method based on 1,800 rental days with a 10% salvage or residual value. Drilling choke controls had been depreciated using 20% declining balance method. Management's operating experience led to the decision to change the number of rental days to 1,575 rental days with a 10% salvage or residual value for the unit-of-use method for electronic drilling recorders and 1,800 rental days with a 10% salvage or residual value and use of the unit-of-use method for drilling choke controls. This change in accounting estimate has been applied prospectively effective January 1, 2002.

Effective July 1, 2002, the undepreciated balance of satellite telephones, which were depreciated as part of the electronic drilling recorders, were reclassified to their own category and are being depreciated on a straight-line basis over 30 months.

The impact of these changes on the year ended December 31, 2002 was to increase depreciation expense by a total of $2,077,907.

5. SIGNIFICANT ACCOUNTING POLICIES

INVENTORY

Inventory is comprised of parts and raw materials awaiting assembly into capital assets. Inventory is recorded at the lower of average cost or replacement cost.

CAPITAL ASSETS

The electronic drilling recorders, owned and under capital lease, are recorded at cost and are depreciated using a unit-of-use method based on 1,575 rental days with a 10% salvage or residual value. Pit volume totalizers, owned and under capital lease, total gas systems and drilling choke controls are recorded at cost and are depreciated using a unit-of-use method based on 1,800 rental days with a 10% salvage value.

All other capital assets, except satellite telephones, are recorded at cost and are depreciated using the declining-balance method at the following annual rates:

Geological services equipment	10%
Trucks	30%
Other	30%

Satellite telephones are recorded at cost and effective July 1, 2002, are depreciated on a straight-line basis over 30 months.

Leasehold improvements are amortized on a straight-line basis over the terms of the leases, which range from two to ten years.

RESEARCH AND DEVELOPMENT

The Company follows the practice of expensing all research expenditures as incurred, net of related investment tax credits. Development costs are expensed as incurred, unless they meet the criteria for deferral and amortization under Canadian generally accepted accounting principles.

Development costs incurred on new product development projects, which, in the Company's view, have clearly defined market prospects are deferred and are amortized over three years commencing in the year in which the new products begin generating rental revenue. However, if at any time that a product is deemed not commercially viable, the balance of its deferred costs will be expensed.

FOREIGN CURRENCY TRANSLATION

The accounts of the Company's self-sustaining foreign operations are translated into Canadian dollars using the current-rate method. Assets and liabilities are translated at the year-end exchange rate and revenues and expenses are translated at average exchange rates. Gains and losses arising from the translation of the financial statements of the foreign operations are deferred in a foreign currency translation adjustment account in shareholders' equity.

GOODWILL

Goodwill is recorded at cost and in accordance with the new accounting recommendation effective January 1, 2002 is not being amortized. The recorded amount of goodwill will be subject to a periodic review to ensure that the fair value remains greater than, or equal to, book value. Any excess of book value over fair value will be charged to income in the period in which the impairment is determined to have occurred.

5. SIGNIFICANT ACCOUNTING POLICIES (continued)

INCOME TAXES

The Company follows the liability method of accounting for income taxes. Under this method, the Company records future income taxes on the effect of any differences between the accounting and income tax basis of an asset or liability. The effect of a change in income tax rates on future income tax liabilities is recognized in income in the period that the change occurs.

USE OF ESTIMATES

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. The most significant of these estimates are related to the amortization period for capital assets and deferred development costs and the provision of doubtful accounts receivable. Actual results could differ significantly from these estimates.

REVENUE RECOGNITION

Revenue is primarily recognized based upon completion of each rental day for rental products or geological services during the reporting period.

6. CAPITAL ASSETS

2002

	COST	ACCUMULATED DEPRECIATION AND AMORTIZATION	NET BOOK VALUE
	$	$	$
Electronic drilling recorders	36,761,332	5,809,110	30,952,222
Electronic drilling recorders under capital lease	10,296,792	1,627,122	8,669,670
Satellite telephones	5,875,654	1,437,829	4,437,825
Pit volume totalizers	9,564,677	2,416,800	7,147,877
Pit volume totalizers under capital lease	2,185,160	552,146	1,633,014
Total gas systems	2,606,233	104,357	2,501,876
Geological services equipment	4,521,592	3,208,128	1,313,464
Electronic drilling choke controls	1,713,400	320,801	1,392,599
Trucks	1,390,765	905,672	485,093
Trucks under capital lease	1,287,797	1,174,106	113,691
Leasehold improvements	4,224,893	1,291,630	2,933,263
Other	6,064,990	3,492,489	2,572,501
	86,493,285	22,340,190	64,153,095

6. CAPITAL ASSETS (continued)

2001

	COST	ACCUMULATED DEPRECIATION AND AMORTIZATION	NET BOOK VALUE
	$	$	$
Electronic drilling recorders	30,655,301	3,604,684	27,050,617
Electronic drilling recorders under capital lease	10,296,792	1,284,160	9,012,632
Satellite telephones	4,779,219	814,520	3,964,699
Pit volume totalizers	8,253,116	1,948,125	6,304,991
Pit volume totalizers under capital lease	2,185,160	515,801	1,669,359
Total gas systems	2,168,807	–	2,168,807
Geological services equipment	4,739,025	2,805,245	1,933,780
Electronic drilling choke controls	1,673,576	458,263	1,215,313
Trucks	1,868,744	1,016,447	852,297
Trucks under capital lease	1,721,700	1,084,984	636,716
Leasehold improvements	2,914,117	954,889	1,959,228
Other	4,855,010	2,467,076	2,387,934
	76,110,567	16,954,194	59,156,373

The depreciation recorded in 2002 was $8,002,055 (2001 – $6,477,077). Included in other assets is the book value of goodwill amounting to $496,957 (2001 – $503,058).

7. DEFERRED DEVELOPMENT COSTS

	2002	2001
	$	$
Cost, beginning of year	**3,945,367**	2,613,503
Additional costs deferred	**1,400,649**	1,331,864
	5,346,016	3,945,367
Accumulated amortization	**(2,035,859)**	(1,125,077)
Balance, end of year	**3,310,157**	2,820,290

The amortization recorded in 2002 was $910,782 (2001 – $863,970).

8. BANK INDEBTEDNESS

The Company's subsidiary, Pason Systems Corp., has a $5,000,000 credit facility, which bears interest at the Canadian bank prime rate plus 0.75%. A general assignment of its accounts receivable is pledged as collateral. At December 31, 2002, an amount of $3,360,000 had been drawn on this credit facility (2001 – $2,610,000).

The Company's U.S. subsidiary has a US$1,500,000 (CDN$2,387,250) revolving line of credit, which bears interest at the United States bank prime rate plus 0.5%. The revolving line of credit requires monthly interest payments and matures July 31, 2004. At December 31, 2002, an amount of US$1,039,589 (CDN$1,634,442) (2001-$nil) was drawn on the line of credit. A general assignment of accounts receivable, capital assets and inventory is pledged as collateral.

9. LONG-TERM DEBT

The Company's U.S. subsidiary has a US$700,000 (CDN$1,101,100) term facility at prime rate plus 0.5% and requires monthly principal payments of US$14,584 (CDN$22,929) plus interest to May 20, 2004. A general assignment of its accounts receivable, capital assets and inventory is pledged as collateral. At December 31, 2002, US$247,896 (CDN$389,742) (2001 – US$422,904 (CDN$673,052)) was outstanding on the term facility. The current portion as at December 31, 2002 was US$175,008 (CDN$275,148).

10. OBLIGATIONS UNDER CAPITAL LEASES

Future minimum payments under capital leases, which includes the buyouts at the end of the leases, where applicable, as at December 31, 2002 and 2001 are as follows:

	2002	2001
	$	$
2002	–	4,075,647
2003	**4,043,625**	4,043,625
2004	**2,772,645**	2,772,645
	6,816,270	10,891,917
Imputed interest on leases at 7% to 9%	**457,536**	1,181,522
	6,358,734	9,710,395
Less current portion	**3,380,966**	3,219,003
	2,977,768	6,491,392

11. SHARE CAPITAL

Authorized
Unlimited number of common shares
Unlimited number of preferred shares
Issued
Common shares

	SHARES	AMOUNT
	#	$
Balance, December 31, 2000	16,788,986	12,266,526
Exercise of employee stock options	663,843	1,797,421
Purchased and cancelled (NOTE 11(B))	(16,800)	(18,312)
Balance, December 31, 2001	17,436,029	14,045,635
Exercise of employee stock options	467,242	2,528,973
Balance, December 31, 2002	17,903,271	16,574,608

a) At December 31, 2002, stock options were outstanding for 1,639,400 common shares at $2.50 to $13.15 per share expiring between July 31, 2003 and December 30, 2007 as follows:

	2002		2001	
	SHARE OPTIONS	WEIGHTED AVERAGE EXERCISE PRICE	SHARE OPTIONS	WEIGHTED AVERAGE EXERCISE PRICE
	#	$	#	$
Outstanding, beginning of year	1,872,142	6.63	1,962,135	4.83
Granted	353,500	12.19	878,250	7.74
Exercised	(467,242)	5.41	(663,843)	2.71
Cancelled	(119,000)	8.61	(304,400)	6.66
Outstanding, end of year	1,639,400	8.04	1,872,142	6.63
Exercisable, end of year	642,650		630,742	
Available for grant, end of year	508,992		220,181	

11. SHARE CAPITAL (continued)

2002

	OPTIONS OUTSTANDING			OPTIONS EXERCISABLE	
RANGE OF EXERCISE PRICE	OPTIONS OUTSTANDING	WEIGHTED AVERAGE REMAINING CONTRACTUAL LIFE	WEIGHTED AVERAGE EXERCISE PRICE	EXERCISABLE (VESTED)	WEIGHTED AVERAGE EXERCISE PRICE
$	#	YEARS	$	#	$
2.50 – 6.00	148,950	0.781	3.57	148,300	3.56
6.01 – 8.00	891,250	3.110	6.94	387,850	6.86
8.01 – 13.15	599,200	4.030	10.77	106,500	8.63
	1,639,400	3.235	8.04	642,650	6.39

The Company accounts for its stock option plan using the intrinsic value of options issued whereby no compensation costs have been recognized in the financial statements for stock options granted to employees and directors. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model, with the following weighted average assumptions used for grants in the year ended December 31, 2002: dividend yield of 0%, expected volatility of 22%, risk-free interest rate of 5.05%, and expected grant life of 4 years. The effect on compensation costs of using this approach has an insignificant impact on the Company's net income and net income per share for the year ended December 31, 2002.

b) Effective October 2, 2000, the Toronto Stock Exchange accepted notice of the Company's intention to make a Normal Course Issuer Bid (the "Bid") through the facilities of the exchange. The Bid commenced on October 4, 2000 and expired on October 3, 2001 and was not renewed. Under the provisions of the Bid, in 2001, the Company purchased 16,800 common shares at an average price of $6.80 per share. The shares have subsequently been cancelled. The cost of the purchases in 2001 was $114,220 of which $18,312 was charged to share capital based on the average book value per share as of the date of purchase, and the remaining $95,908 was charged to retained earnings.

12. INCOME TAXES

The provision for income taxes reflects an effective income tax rate, which differs from the combined federal and provincial statutory rates of 39.6% for 2002 and 41.6% for 2001. As well, Pason Systems USA Corp. has federal and state statutory tax rates of 40% for 2002 and 2001. The main differences are as follows:

12. INCOME TAXES (continued)

	2002	2001
	$	$
Earnings before income taxes	**15,728,647**	26,731,643
Expected income taxes	**6,192,857**	11,125,709
Increase (decrease) resulting from:		
Other non deductibles	**196,239**	60,135
Foreign income tax rates	**(180,838)**	(293,144)
Non-taxable dividends	**(102,737)**	–
Share issuance deductions	–	(62,095)
Other	**16,787**	463,751
Income tax expense	**6,122,308**	11,294,356

The Company has future income tax liabilities related to temporary differences between the book value and the tax value of the capital assets in the amount of $6,268,049 (2001 – $6,284,059).

13. FINANCIAL INSTRUMENTS

The fair value of financial instruments, which include accounts receivable, inventory, bank indebtedness, accounts payable and accrued liabilities, long-term debt and obligations under capital leases approximates amounts at which these instruments could be exchanged in a transaction between knowledgeable and willing parties.

The Company is exposed to credit risk to the extent that its customers may experience financial difficulty and would be unable to meet their obligations. However, the Company has a large number of customers, which minimizes concentration of credit risk.

Obligations under capital leases carry interest at rates that are not significantly different from year-end interest rates. Consequently, the fair value of these long-term liabilities approximates their carrying value.

Long-term debt is based on prime rate interest rates. As a result of fluctuations to prime rates, the Company is exposed to varying interest rate risks.

14. PER SHARE AMOUNTS

Earnings per share have been calculated using the weighted average number of common shares outstanding during the year, which amounted to 17,747,752 shares (2001 – 17,147,210). Diluted amounts per share have been calculated using the weighted average number of common shares and dilutive equity instruments of 18,275,716 (2001 – 17,539,062).

Historical Review

SELECTED FINANCIAL DATA

YEARS ENDED DECEMBER 31,	2002	2001	2000	1999	1998	1997	1996
(000S, EXCEPT PER SHARE AMOUNTS)	$	$	$	$	$	$	$
OPERATING RESULTS							
Revenue	**55,311**	63,016	42,144	24,668	23,768	14,496	4,497
Expenses							
Rental services	**17,088**	13,641	9,290	5,649	4,830	2,348	1,029
Geological services	**4,608**	6,262	5,326	3,852	3,568	911	–
Shop	**2,359**	2,551	1,900	1,426	1,125	740	298
Administration	**2,498**	2,415	2,826	1,867	1,631	702	441
Research & development	**3,009**	2,750	2,006	1,403	967	508	222
Depreciation & amortization	**8,913**	7,341	5,340	2,898	2,584	1,689	580
Net earnings	**9,606**	15,437	8,117	4,084	4,900	4,102	909
Per share – basic	**0.54**	0.90	0.49	0.25	0.30	0.29	0.07
Cash flow from operations	**18,534**	24,941	14,797	7,966	7,417	6,014	1,537
Per share – basic	**1.05**	1.45	0.89	0.49	0.47	0.43	0.11
EBITDA	**25,750**	35,396	20,797	10,511	11,686	9,275	2,332
Per share – basic	**1.45**	2.06	1.25	0.65	0.73	0.66	0.19
Capital expenditures	**14,732**	22,921	23,419	10,851	8,294	7,957	2,438
FINANCIAL POSITION							
Current assets	**22,728**	20,276	18,150	11,461	10,470	10,529	3,028
Total assets	**90,191**	82,252	64,451	40,193	30,736	25,179	7,346
Working capital	**7,775**	5,135	1,416	3,283	5,769	3,824	600
Long-term debt	**115**	395	635	–	–	233	364
Future income tax	**6.268**	6,284	3,800	2,159	1,030	860	81
Shareholders' equity	**65,878**	53,941	35,448	26,261	22,639	16,878	3,979
Return on shareholders' equity	**16%**	35%	26%	17%	24%	41%	43%
COMMON SHARE DATA							
Common shares outstanding (#)							
At December 31	**17,903**	17,436	16,789	16,296	16,169	15,900	13,721
Weighted average	**17,748**	17,147	16,604	16,257	16,103	14,058	12,412
Share trading							
High ($)	**13.35**	10.34	9.75	6.90	8.50	6.50	2.40
Low ($)	**8.65**	6.00	5.50	2.25	2.50	6.30	0.70
Close ($)	**11.95**	9.10	6.95	6.25	2.90	6.50	2.15
Volume (#)	**5,479**	4,423	3,233	3,266	4,987	4,422	n/a

Corporate Information

OFFICERS AND KEY PERSONNEL

Pason Systems Inc.

JIM HILL
PRESIDENT & CHIEF EXECUTIVE OFFICER

JOANNE DICKIE
CHIEF FINANCIAL OFFICER

Pason Systems Corp.

JIM HILL
PRESIDENT

JOANNE DICKIE
CHIEF FINANCIAL OFFICER

LUCY TOMIE
CONTROLLER

BOB RODDA
CANADIAN BUSINESS UNIT MANAGER

DAVID WHITE
R&D MANAGER

JAMES PARKS
MANUFACTURING MANAGER

Pason Systems USA Corp.

JIM HILL
PRESIDENT

BEN THOMAS
U.S. BUSINESS UNIT MANAGER

JERRY ABERLE
CHIEF FINANCIAL OFFICER

JOE WATSON
GEOLOGICAL SERVICES MANAGER

CORPORATE HEAD OFFICE

PASON SYSTEMS INC.
6130 THIRD STREET S.E.
CALGARY, ALBERTA, CANADA T2H 1K4
TELEPHONE: (403) 301-3400
FACSIMILE: (403) 301-3499
WEBSITE: www.pason.com
E-MAIL: info@pason.com

AUDITORS

DELOITTE & TOUCHE LLP
CALGARY, ALBERTA

BANKER

ROYAL BANK OF CANADA
CALGARY, ALBERTA

LEGAL COUNSEL

GOWLING LAFLEUR HENDERSON LLP
CALGARY, ALBERTA

REGISTRAR AND TRANSFER AGENT

Inquiries regarding change of address, registered shareholdings, stock transfers or lost certificates should be directed to:

VALIANT TRUST COMPANY
SUITE 510, 550 SIXTH AVENUE S.W.
CALGARY, ALBERTA T2P 0S2
TELEPHONE: (403) 233-2801

STOCK TRADING

TORONTO STOCK EXCHANGE
TRADING SYMBOL: PSI

ANNUAL MEETING

The Annual Meeting of Shareholders of Pason Systems Inc. will be held on Monday, June 2, 2003 at 3:30 p.m. (Calgary time) in the offices of Pason Systems Inc., 6130 Third Street S.E., Calgary, Alberta. Shareholders who are unable to attend the Meeting are requested to complete and return the Instrument of Proxy to Valiant Trust Company at their earliest convenience.

Directors Sound corporate governance, which is the responsibility of the Company's Board of Directors and its associated committees, promotes and protects the interests of all Pason shareholders. It is charged with providing strategic direction for management's activities, approving all major business decisions and monitoring the Company's ongoing performance.

Pason's Board is comprised of a diverse group of highly skilled professionals with extensive knowledge and expertise in all aspects of business and finance. Each member brings to Pason an unwavering level of dedication, enthusiasm and support, as well as a pledge to work with the Company's management to fulfill shareholders' expectations through sound, ethical business practices.

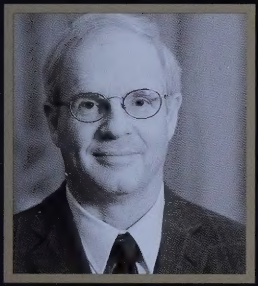
HAROLD R. ALLSOPP, MBA, CA
PRESIDENT
HABEDE HOLDINGS LTD.
CALGARY, ALBERTA
(1)(2)

As President of Habede Holdings Ltd., an investment and consultancy firm, Mr. Allsopp has been serving his local, national and international clients for over 13 years. Formerly, he served as Vice-President, Finance for Voyager Energy Inc. and Canadian Hydrocarbons Ltd., and worked with Ernst & Young in both auditing and consultancy capacities. Mr. Allsopp is a board member of several private and public corporations.

MURRAY L. COBBE
Eng.Diploma (Petroleum)
PRESIDENT &
CHIEF EXECUTIVE OFFICER
TRICAN WELL SERVICE LTD.
CALGARY, ALBERTA
(1)(3)

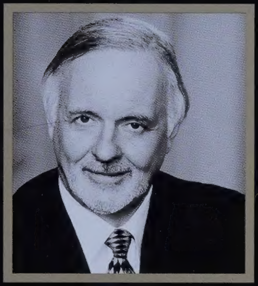
Mr. Cobbe has been in the well services business since 1974 having overseen operations in Canada, Europe, the Middle East and the United States. Mr. Cobbe has served as President and Chief Executive Officer of Trican Well Service Ltd. since its successful IPO in 1996 and is a director of the Petroleum Services Association of Canada as well as Great Northern Exploration Ltd.

DIRECTORS



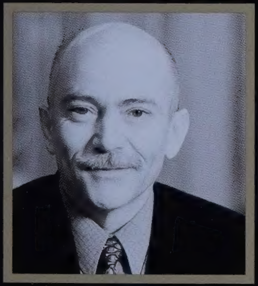
JAMES D. HILL, Ind.Eng., CA
PRESIDENT &
CHIEF EXECUTIVE OFFICER
PASON SYSTEMS INC.
CALGARY, ALBERTA

Since 1986 when he purchased the Company from Badger Drilling Ltd., a drilling contractor, Mr. Hill has been President and Chief Executive Officer as well as principal shareholder of Pason. Mr. Hill served as Secretary-Treasurer of Badger for six years and prior thereto as an audit manager with the accounting firm Ernst & Young. With over 30 years experience and leadership in all aspects of finance and the oilfield service sector, Mr. Hill offers tremendous industry knowledge and foresight to both Pason and its shareholders.



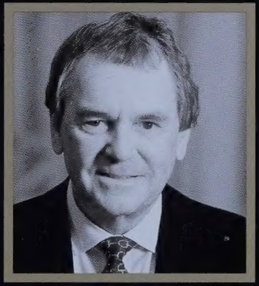
PAUL F. LITTLE, MBA
PRESIDENT
WESTOVER INVESTMENTS INC.
CALGARY, ALBERTA
(2)(3)

Mr. Little has served as President of Westover Investments Inc. since 1999, following 13 years as a principal of the Toronto-based merchant banking firm Gornitzki, Thompson & Little, and formerly as Vice-President and Chief Financial Officer for Union Gas Limited. Mr. Little serves on the boards of numerous public companies.



JAMES B. HOWE, CA
PRESIDENT
BRAGG CREEK FINANCIAL CONSULTANTS LTD.
CALGARY, ALBERTA
(1)(2)

Mr. Howe is President of Bragg Creek Financial Consultants Ltd., a private consulting company. Mr. Howe has extensive public company experience having served as an officer or director of numerous public oil and gas producers and service companies. Mr. Howe currently serves as a director of Argo Energy Inc., Ensign Resource Service Group Inc. and Wrangler West Energy Corp., and is Vice-President Finance, Chief Financial Officer and a director of Kinloch Resources Inc.



PETER S. MACKECHNIE, CA
ASSOCIATE DIRECTOR
BEAR STEARNS
LOS ANGELES, CALIFORNIA
(3)

Since joining Bear Stearns in 1989, Mr. Mackechnie has served as Associate Director based in Los Angeles. Prior thereto, he was President of Harvest Management Inc., a Denver-based investment advisory firm.

(1) Audit Committee Member
(2) Compensation Committee Member
(3) Corporate Governance Committee Member

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